



DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 203

**Docket No. FR-5397-N-05
RIN 2502-ZA05**

**Federal Housing Administration (FHA):
Temporary Waiver of FHA's Regulation on Property Flipping
Extension of Waiver**

AGENCY: Office of the Assistant Secretary for Housing – Federal Housing Commissioner, HUD.

ACTION: Notice of waiver extension.

SUMMARY: This notice of waiver extension announces that FHA is extending the availability of the temporary waiver of its regulation that prohibits the use of FHA financing to purchase single family properties that are being resold within 90 days of the previous acquisition, until December 31, 2014. This waiver, which was first issued in January 2010, took effect for all sales contracts executed on or after February 1, 2010. On January 28, 2011, FHA extended the waiver through calendar 2011. On December 28, 2011, FHA extended the waiver through calendar 2012. Prior to the waiver, a mortgage was not eligible for FHA insurance if the contract of sale for the purchase of the property that secured the mortgage was executed within 90 days of the prior acquisition by the seller, and the seller did not come under any of the exemptions to this 90-day period specified in the regulation.

Through the regulatory waiver, FHA encourages investors that specialize in acquiring and renovating properties to renovate foreclosed and abandoned homes, with the objective of increasing the availability of affordable homes for first-time and other purchasers, helping to stabilize real estate prices as well as neighborhoods and communities where foreclosure activity

has been high. The waiver is applicable to all single family properties being resold within the 90-day period after prior acquisition, and is not limited to foreclosed properties. Additionally, the waiver is subject to certain conditions, and mortgages must meet these conditions to be eligible for the waiver. The waiver is not applicable to mortgages insured under HUD's Home Equity Conversion Mortgage (HECM) Program.

DATES: Effective Date: January 1, 2013 through December 31, 2014.

FOR FURTHER INFORMATION CONTACT: Karin B. Hill, Director, Office of Single Family Program Development, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Washington, DC 20410-8000; telephone number 202-708-2121 (this is not a toll-free number). Persons with hearing or speech impairments may access this number through TTY by calling the toll-free Federal Relay Service at 800-877-8339.

SUPPLEMENTARY INFORMATION:

I. Background

Section 203.37a(b)(2) of HUD's regulations (24 CFR 203.37a(b)(2)) establishes FHA's rule on recent resales of single family properties; this regulatory section provides that FHA will not insure a mortgage for a single family property if the contract of sale is executed within 90 days of the acquisition of the property by the seller. The acquisition date is the date that seller has the power, under the law of the state in which the property is located, to transfer title to a buyer. Section 203.37a(c) lists the sales transactions that are exempt from this rule. The exempt transactions include sales by HUD of real estate-owned (REO) properties under HUD's regulations in 24 CFR part 291, sales by other federal agencies of REO properties, sales of properties by nonprofit organizations that have been approved to purchase and resell HUD REO

properties, and sales by state- and federally-chartered financial institutions and government sponsored enterprises (GSEs).

“Property flipping” refers to the practice in which a property recently acquired is resold for a considerable profit with an artificially inflated value, often as the result of a lender’s collusion with an appraiser. Most property flipping occurs within a matter of days after acquisition, and usually with only minor cosmetic improvements, if any, to the property. In an effort to preclude this predatory lending practice with respect to mortgages insured by FHA, HUD issued a final rule on May 1, 2003 (68 FR 23370) that provides in 24 CFR 203.37a that FHA will not insure a mortgage if the contract of sale for the purchase of the property that secures the mortgage is executed within 90 days of the prior acquisition by the seller, and the seller does not come under any of the exemptions to this 90-day period specified in § 203.37a(c).

In a final rule published on June 7, 2006 (71 FR 33138), HUD expanded the exemptions to the 90-day time restrictions contained in § 203.37a(c) to include transactions such as sales of single family properties by GSEs, state- and federally-chartered financial institutions, nonprofit organizations approved to purchase HUD REO single family properties at a discount with resale restrictions, local and state governments and their instrumentalities, and, upon announcement by HUD through issuance of a notice, sales of properties in areas designated by the President as federal disaster areas.

The downturn in the housing market over the past several years led to a rapid rise of homeowners defaulting on mortgages, and consequently an increase in vacant foreclosed homes. Federal, state, and local governments initiated a variety of measures to avoid foreclosures. Although these efforts to keep families in their homes have helped to improve the condition of the housing market, the foreclosure rate remains unacceptably high. Not only do foreclosures

affect the families that lost their homes, but they affect neighborhoods and communities. While HUD continues its efforts to help homeowners remain in their homes, through the waiver of its regulation on property flipping, HUD seeks to help stabilize neighborhoods and communities.

HUD first granted temporary waiver of its regulation on anti-property flipping through notice published in the Federal Register on May 21, 2010, at 75 FR 28633. The May 2010 notice waived HUD's regulations through December 31, 2011. Through notice of waiver extension published in the Federal Register on December 28, 2011, at 76 FR 81363, HUD extended the waiver through December 31, 2012. Through this notice of waiver extension published in today's edition of the Federal Register, HUD announces the extension of the waiver through December 31, 2014. HUD is cognizant of concerns expressed by industry, state and local jurisdictions, and other interested parties that they receive sufficient advance notice by HUD of any planned extension of the waiver, which they advise was not the case in the extension of waiver through the end of calendar year 2012. For this reason, HUD is providing notice of the extension of the waiver through December 31, 2014, well in advance of December 31, 2012.

Since the waiver was made available, HUD believes that it has made a significant contribution to neighborhood stabilization. While the waiver remains available for the purpose of stimulating rehabilitation of foreclosed and abandoned homes for two more calendar years, the waiver continues to remain applicable to all properties being resold within the 90-day period after prior acquisition. The waiver is not limited to the resale of foreclosed properties.

II. Eligibility for Waiver of 24 CFR 203.37a(b)(2)

To be eligible for the waiver of the Property Flipping Rule, an FHA-approved mortgagee must ensure that the mortgage meets the following conditions:

1. All transactions must be arms-length, with no identity of interest between the buyer and seller or other parties participating in the sales transaction. Some ways that the lender may ensure that there is no inappropriate collusion or agreement between parties, are to assess and determine the following:

- a. The seller holds title to the property;
- b. Limited liability companies, corporations, or trusts that are serving as sellers were established and are operated in accordance with applicable state and federal law;
- c. No pattern of previous flipping activity exists for the subject property as evidenced by multiple title transfers within a 12 month time frame (chain of title information for the subject property can be found in the appraisal report);
- d. The property was marketed openly and fairly, through a multiple listing service (MLS), auction, for sale by owner offering, or developer marketing (any sales contracts that refer to an “assignment of contract of sale,” which represents a special arrangement between seller and buyer may be a red flag).

2. In cases in which the sales price of the property is greater than 20 percent above the seller’s acquisition cost, the mortgage is eligible for the waiver only if the mortgagee:

- a. Justifies the increase in value by retaining in the loan file a second appraisal and/or supporting documentation, which verifies that the seller has completed sufficient legitimate renovation, repair, and rehabilitation work on the subject property to substantiate the increase in value or, in cases where no such work is performed, the appraiser provides appropriate explanation of the increase in property value since the prior title transfer; and
- b. Orders a property inspection and provides the inspection report to the purchaser before closing. The mortgagee may charge the borrower for this inspection. The use of FHA-approved

inspectors or 203(k) consultants is not required. The inspector must have no interest in the property or relationship with the seller, and must not receive compensation for the inspection for any party other than the mortgagee. Additionally, the inspector may not: compensate anyone for the referral of the inspection; receive any compensation for referring or recommending contractors to perform any repairs recommended by the inspection; or be involved with performing any repairs recommended by the inspection. At a minimum, the inspection must include:

- i. The property structure, including the foundation, floor, ceiling, walls and roof;
- ii. The exterior, including siding, doors, windows, appurtenant structures such as decks and balconies, walkways and driveways;
- iii. The roofing, plumbing systems, electrical systems, heating and air conditioning systems;
- iv. All interiors; and
- v. All insulation and ventilation systems, as well as fireplaces and solid fuel-burning appliances.

3. Only forward mortgages are eligible for the waiver. Mortgages insured under HUD's HECM program are ineligible for the waiver.

III. Guidance on the Conditions for Waiver Eligibility

A. Seller's Acquisition Cost

The seller's acquisition cost is the purchase price which the seller paid for the property, and the following costs (if paid by the seller):

- Closing costs, plus
- Prepaid costs, including commissions.

The seller's acquisition cost does not include the cost of repairs that the seller makes to the property.

B. Justification and Documentation of Increase in Value

If the resale price of the property is greater than 20 percent above the seller's acquisition cost, the mortgage will be eligible for FHA insurance only if the mortgagee justifies the increase in value. The mortgagee must verify that the seller has completed sufficient legitimate renovation, repair, or rehabilitation work on the subject property to substantiate the increase in value by retaining supporting documentation in the loan file or by providing a second appraisal.

- If the mortgagee uses a second appraisal:
 - An FHA roster appraiser must perform the appraisal in compliance with all FHA appraisal reporting requirements.
 - The mortgagee may not use an appraisal done for a conventional loan even if it was completed by an FHA roster appraiser.
 - The mortgagee may not charge the cost of the second appraisal to the homebuyer.

If the mortgagee has ordered a second appraisal to document the increase in value, the mortgagee must not use this appraisal for case processing and must not enter it into FHA Connection.

C. Property Inspection Report

If the resale price of the property is greater than 20 percent above the seller's acquisition cost, the mortgage will be eligible for FHA insurance only if the mortgagee obtains a property inspection and provides the inspection report to the buyer before closing. The borrower, lender,

or mortgage broker (if one is involved in the transaction) may order the property inspection. The lender or mortgage broker may charge the borrower for this inspection.

D. Repairs

If the inspection report notes that repairs are required because of structural or “health and safety” issues, those repairs must be completed prior to closing. After completion of repairs to address structural or “health and safety” issues, the inspector must conduct a final inspection to determine if the repairs have been completed satisfactorily and eliminated the structural or “health and safety” issues. The borrower, lender, or mortgage broker may order the final inspection.

IV. Compliance with the Paperwork Reduction Act

The information collection requirements applicable to this waiver have been submitted to the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB Control No. 2502-0059. In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection displays a currently valid OMB control number.

VI. Period of Waiver Eligibility

The waiver that is the subject of this notice remains effective beyond December 31, 2012, through December 31, 2014, for all sales contracts executed on or after February 1, 2010, the availability date provided by the issuance of the waiver in January 2010, unless extended or withdrawn by HUD.

By notice, HUD shall notify the public of any extension or withdrawal of this waiver. If as a result of this waiver, there is a significant increase in defaults on FHA-insured mortgages

and an increase in mortgage insurance claims that are attributable to mortgages insured as a result of exercise of this waiver authority, HUD may withdraw this waiver immediately.

Dated: November 26, 2012

Carol J. Galante
Acting Assistant Secretary for Housing—
Federal Housing Commissioner

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